

*As Seen In*  
**CALIFORNIA  
BROKER**

by Jim Passarelli

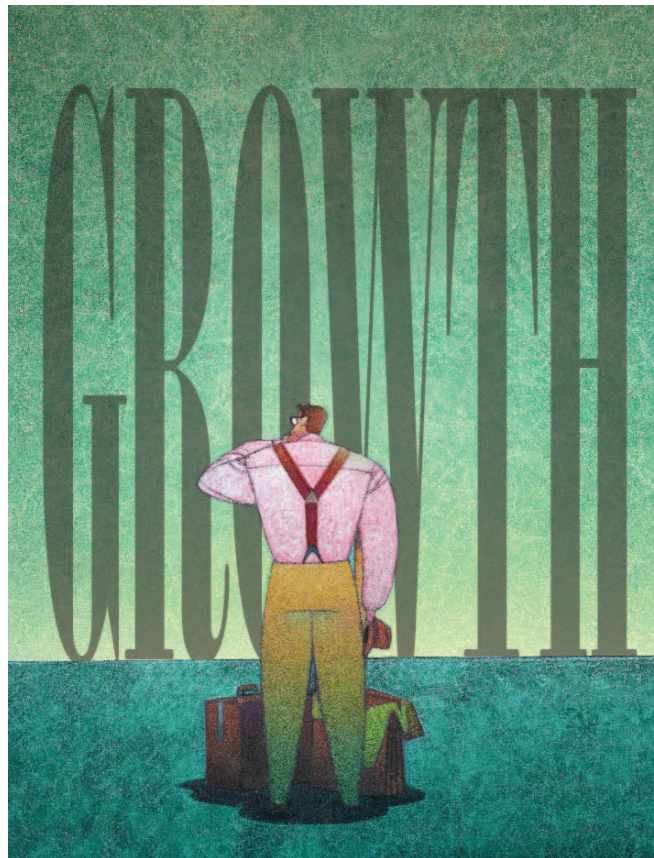
The life settlement marketplace has been growing exponentially since its creation in the late 1990's. Many factors have supported this growth and many emerging trends and developments should propel life settlement transactions to ever-increasing levels in the future. Since life settlements have proven to be pro-consumer, they are getting increasing attention from advisors, agents, CPAs, lawyers, and trust officers who find them useful in the right situations. Several emerging trends bode well for life settlements and promise to increase their interest and use as a new and effective financial tool.

The sheer volume of seniors who will be entering retirement age at the end of this decade represents the largest demographic group of people in U.S. history. Baby Boomers are poised to begin retirement at the end of the decade and will continue to retire for the next 18 years. It is interesting to note that the birth and phenomenal growth of the life settlement market took place along with one of the smallest groups of retirees -- those born in the 1930s. The growing focus on fulfilling fiduciary duty is also leading advisors to review the often-overlooked insurance policy in a new light. Once believed to be an unchangeable asset with few options, advisors now see the possibility of great value in their client's insurance policies.

Increased state regulation has also helped define the legal roles and duties of brokers, agents, and funders in the life settlement transaction, while preserving the consumers right to protection and regulation. This structure and regulation has helped set standards and encourage confidence in secondary insurance market transactions.

Those who were prepared to pay large estate tax bills with large life insurance

# Growth is on the Horizon for Life Settlements



policies are encouraged to consider selling those policies as estate taxes continue to decline. Increased competition, cost savings through insurance industry mergers and acquisitions, and revised mortality tables have brought about aggressive new premiums and riders, making many current insurance policy and rider choices more cost effective than those currently in-force. Also, the growing acceptance of life settlements and the increasing information about them have helped advisors make informed decisions.

## The Growing Senior Population

By definition, life settlements are performed for life insurance policyholders who are 65 and older. So, it is important

to consider the senior landscape, which will be changing dramatically. There has been tremendous life settlement growth over the past six years in a historically small senior market due to low birth rates in the late 1920s and early 1930s. The silent generation, those currently age 63 to 80, is a much smaller demographic group compared to the Baby Boomers, which will begin retiring at the end of the decade. The number of seniors in the marketplace will only increase from this point on, presenting more opportunities for life settlements. As those in the largest popula-

tion boom in U.S. history begin to retire, they will begin to position themselves and their assets for retirement. Protecting themselves financially and replacing lost work income will become a priority to seniors. Many will choose to sell life insurance policies to help accomplish that goal.

## Increased Focus on Fiduciary Duties

Advisors are more concerned than ever with fulfilling their fiduciary duty to clients. As of 2003, 41 states adopted the Uniform Prudent Investor Act, which is helping define fiduciary duty and how it applies. Whether held by trust, individual, business, group, or charitable organization, life insurance

policies are receiving new and more intense scrutiny. The life insurance policy was once an asset that was considered unchanging or of no liquid value, but is now being considered as part of the client portfolio.

As regulation has come into place, the portfolio embraces all items managed, including insurance. Life insurance review and valuation is now falling under the fiduciary duty of advisors and trust officers. Life insurance is now being included in regular assessments and reviews along with all other assets. "Internal and external situations may change, coverage may no longer be appropriate, or similar coverage may be available with a substantially reduced premium. Either way, a life insurance valuation should be performed periodically on all eligible life insurance policies," says John E. Mayer CFP AIFA of Fiduciary Review Services. Advisors who want to exercise due care and skill are ensuring that any life insurance policies that are in their client's possession are included in regular reviews. It is important to note that, with the emergence and growth of the life settlement marketplace, a system to evaluate policies has evolved along with the increased requirement of insurance review and assessment.

### Increased Regulation

The National Assn. of Insurance Commissioners (NAIC) and The National Conference of Insurance Legislators (NCOIL) have developed model acts pertaining to life settlements. Also, 36 states have adopted some form of regulation to ensure the consumer's right to sell a policy in the secondary insurance marketplace and be protected when doing so. State government recognition and regulation has aided the market by defining business practices, standards, and licensing, which gives insurance policy holders confidence and protects all involved.

### Uncertainty With Estate Tax

Uncertainty with estate tax has led to a rethinking of tax strategy. As estate-tax rates continue to fall, the life insurance policies put in place to offset estate taxes may no longer be needed.

Many advisors had rightly put life

insurance policies in place to help ensure that their clients could pass their estates intact from one generation to the next. However, such financial mechanisms may no longer be necessary with the changing financial and tax landscape. Estate taxes will decrease and eventually disappear by 2010. It remains to be seen whether Congress will act to make these changes permanent. The current estate-tax reduction is generating life settlement transactions as advisors and clients sell insurance policies that were put in place to cover larger estate tax burdens. The proceeds from the sales are being used for annuities or other income-generating purposes. This trend will only increase if the changes are made permanent.

On the other hand, if estate-tax laws are reenacted, the proceeds from life settlement transactions may be used in a different way. Many single life insurance policies held in trust may be sold. The proceeds will be used to purchase second-to-die policies, which offer comparable coverage, typically lower premiums, and the possibility of insurance coverage on a previously uninsurable person. These second-to-die policies will be placed in irrevocable life insurance trusts (ILIT). One thing is for sure, estate-tax exemptions are changing and these changes will eventually increase life settlement transactions.

### More Competitive Life Insurance

Life insurance products of the past may not be as competitive as new products on the horizon. Increased consolidation and competition in the insurance marketplace are forcing insurance carriers to cut costs and price their products more competitively. In addition, new mortality tables have been introduced for the first time since 1980. These tables extend final maturity on life insurance from 100 to 120 and increase the average life expectancy for females from 77 to 79 and for males from 70 to 74. This should also help reduce premiums, primarily on term insurance, and help make level product available at higher ages and for longer periods.

The traditional insurance reserves that carriers must set aside will be reduced by 20% on average. In turn, smaller reserves

for insurers will mean lower prices. Decreased surrender charges and increased surrender values are expected, which should also help make new policies more attractive. All of these factors combine to increase the attractiveness of a new insurance policy.

### Growth of the Life Settlement Marketplace

The past six years have seen tremendous growth in the life-settlement marketplace. Many institutional investment firms and banks have become involved one way or another including Merrill Lynch, American International Group, Chase Manhattan Bank, Lloyds of London, and HVB Fonds Finance -- to name a few. The secondary insurance marketplace has grown from \$200 million in face amount to over \$2 billion in 2003 -- with future growth projections at 20% a year. Increased growth and competition will spur better service and support. As more professionals incorporate life settlements into their practice, client introduction tools will become an important factor to agents performing settlement transactions. Agents and advisors should expect an increase in tools, support materials, training, E&O coverage, and a competitive multi-bid process. This will promote increasing integration of life settlements into professional practices, streamline the life-settlement process, and return multiple bids on client policies.

In conclusion, ever-increasing numbers of seniors are heading toward retirement; the uncertainty in estate tax law remains; and more competitive insurance rates are emerging from the insurance industry. These trends are bringing agents a large customer base, attractive products, and growing opportunities to conduct life settlements. Growing focus on fiduciary duty and increased regulation will help guide agents and advisors as they investigate and conduct life settlements. All the while, maturing life settlement companies will offer more support and multiple offers. □

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